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SUBJECT: SOUTH AFRICA: DRAFT BEE CODE 500: PREFERENTIAL
PROCUREMENT

REF: (A) PRETORIA 4854
(B) PRETORIA 4855
(C) PRETORIA 4856
(D) PRETORIA 337
(E) PRETORIA 575
(F) PRETORIA 646

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[¶1.](#) (U) Summary. The South African Department of Trade and Industry (DTI) released for public comment drafts of Broad-based Black Economic Empowerment (BEE) Codes of Good Practice belonging to the second and final phase on December 20, 2005. The Minister of Trade and Industry plans to promulgate both the first (which have been finalized) and the second phases of the BEE Codes of Good Practice before the end of 2006. Included in the second phase is Code 500. This code accounts for 20% of the BEE scorecard and sets forth the scoring criteria for firms striving to comply with BEE objectives as they relate to preferential procurement. In each instance, the actual number of points awarded is calculated by multiplying the fraction of a compliance target (Code 500 has three) achieved by the number of possible points allotted for each target. In a recent meeting of their BEE Committee, members of the local American Chamber of Commerce voiced a number of concerns about this draft statement. Comments on all BEE codes of good practice belonging to the second phase must be submitted to DTI by March 31 2006. End Summary.

[¶2.](#) (U) On December 20 2005, the South African Department of Trade and Industry (DTI) released for public comment drafts of BEE Codes of Good Practice belonging to the second and final phase. Comments on these draft codes must be submitted to DTI by March 31 2006. While the BEE Codes of Good Practice belonging to the first phase have been finalized (Refs A, B, and C), the Minister of Trade and Industry will not promulgate them until the codes belonging to the second phase have also been finalized. DTI wants this to occur before the end of [¶2006](#).

[¶3.](#) (U) Codes belonging to the second phase deal with

employment equity (Code 300), skills development (Code 400), preferential procurement (Code 500), enterprise development (Code 600), residual contributions (Code 700), and small and medium sized enterprises (code 1000 - 1700). Also included in the second phase are subsections to Codes 000 (the BEE Framework for Measurement) and 100 (BEE Equity). The two subsections for Code 000 deal with misrepresenting BEE status (Statement 001) as well as and verification issues relating to complex structures (Statement 002). The four subsections for Code 100 deal with guidelines for the recognition of BEE ownership by BEE targeted warehouse funds (Statement 102), multinational companies (Statement 103), public entities and organs of the state (Statement 104), and companies limited by guarantee and Section 21 (i.e. nonprofit) companies (Statement 105). All may be sourced from DTI's website: www.thedti.gov.za.

¶4. (U) This cable focuses on draft Code 500, which sets forth the scoring criteria for firms striving to comply with BEE objectives as they relate to preferential procurement, or purchasing and supply. Septels and reflets report on the other codes.

CODE 500

¶5. (U) Draft Code 500 establishes three compliance targets pertaining to purchasing and supply for firms. Total points account for 20% of the BEE scorecard. For each target, the actual number of points awarded is

PRETORIA 00000700 002 OF 003

calculated by multiplying the fraction of a compliance target achieved by the number of possible points allotted for each target. Excess scoring for exceeding any of the preferential procurement targets is not possible. For a complete understanding as to how this portion of the generic scorecard factors into the rest of the scorecard, please refer to Ref A.

¶6. (U) As set forth in draft Code 500, a firm can score fifteen points if 70% of its total purchases qualify as a "BEE procurement spend" (see paragraphs 7 and 8). A firm can score four points if 15% of its total purchases qualify as a "BEE procurement spend" from small suppliers. A firm can score one point if 5% of its total purchases qualify as a "BEE Procurement Spend" from micro enterprise suppliers.

¶7. (U) "BEE procurement spend" is calculated by multiplying the total value of a firm's purchases from a supplier by that supplier's "BEE procurement recognition level." Every firm's "BEE procurement recognition level" depends upon its overall BEE scorecard performance. For a clear understanding as to how a firm's BEE status and "BEE procurement recognition level" are determined, please refer to Ref A. As established by the BEE Framework (Code 000), the chart below sets forth "BEE procurement recognition levels" for firms with scoring between 0 and 100 points on the BEE scorecard.

BEE Status	Qualification	BEE Procurement Recognition
Level 1 Contributor	100+ points	135%
Level 2 Contributor	85-99 points	125%
Level 3 Contributor	75-84 points	110%
Level 4 Contributor	65-74 points	100%
Level 5 Contributor	55-64 points	80%
Level 6 Contributor	45-54 points	60%
Level 7 Contributor	40-44 points	50%
Level 8 Contributor	30-39 points	10%

Non Compliant 0-29 points 0%

¶8. (U) For example, if a firm purchases goods or services from a Level 3 Contributor, it would multiply the value of its purchase by 110% to arrive a figure, referred to as its "BEE procurement spend." Because preferential procurement will be factored throughout the supply chain, from first tier suppliers to government, the practical effect is that, to stay competitive, all firms will have to take BEE into account in their transactions for both government and non-government business. In this way, the government ensures that its BEE policies pervade the entire value chain to create immediate access to the mainstream economy for increasing numbers of "previously disadvantaged individuals".

¶9. (U) Draft Code 500 allows a firm purchasing goods and services directly from a supplier that benefited from BEE enterprise development (as set forth by Code 600, septel) to recognize these purchase at a multiple of 1.2 when calculating "BEE procurement spend." Draft Code 500 also allows for the exclusion of up to 25% of total purchases for imports that are not locally available.

¶10. (U) The following table lists criteria, points, and targets for deriving a preferential procurement score:

Criteria	Points	Target
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		% of procurement
BEE procurement spend from suppliers based on the BEE procurement recognition levels	15	70%

BEE procurement spend from small	4	15%
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PRETORIA 00000700 003 OF 003

enterprises based on the BEE procurement recognition levels

BEE procurement spend from micro enterprises based on the BEE procurement recognition levels	1	5%
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CONCERNS

¶11. (SBU) On February 8, members of the BEE Committee of the local American Chamber of Commerce met to discuss draft Code 500. Members noted that the target of 70% for purchasing BEE goods was onerous at best. At worst, it was a trade barrier. While the draft code allowed for the exclusion from the calculation of "BEE procurement spend" imports of up to 25% of purchasing and supply, this was not enough and could be interpreted as discrimination against imports. Further, the draft code mandates that if local products were available, then firms must source these products locally. In a subsequent meeting at AmCham on February 15, DTI Director for BEE Jeffrey Ndumo clarified that, indeed, lower foreign prices, long standing customer relationships, product quality, or brand preferences were not acceptable reasons as to why a company should import a product that was locally available. "That was our intent," he said "that companies should buy South African." He further explained, "If the local price is too high, then companies should work with local companies to help them bring their prices down," he explained. Members commented that this would greatly affect multinationals, most of which relied on corporate headquarters to manage purchasing. A large automobile manufacturer explained that his headquarters purchased almost all parts for assembly from original equipment

manufacturers overseas, and that these purchases were coordinated at a global level. Everyone agreed that purchasing from local sources and from smaller firms would likely lead to higher costs and diminished competitiveness. If anything, local firms would not be able to match the production runs of their international competitors and, therefore, unit costs would be higher. On February 15 when this point was raised, Ndumowas unfazed.

Pertinent Definitions

¶12. (U) Code 000 defines "black" as black, coloured," and Indian South Africa citizens (or those who could have applied for South African citizenship, if permitted) who suffered or whose descendants suffered discrimination under the apartheid regime.

13.(U) "Micro Enterprise" is defined as having an annual turnover of less than R300 thousand.

14.(U)"Small enterprise" is defined as having less than 50 employees and depending on the sector in which it operates, an annual turnover of less than R25 million.

¶15. (U) "BEE procurement spend" and "BEE procurement recognition level" are defined and illustrated in Paragraphs 7 and 8.